

STATE OF ALABAMA
DEPARTMENT OF REVENUE,

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STATE OF ALABAMA
DEPARTMENT OF REVENUE
ADMINISTRATIVE LAW DIVISION

§

v.

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DOCKET NO. S. 89-213

CORNERSTONE MEDICAL, INC.
1225 Johnson Ferry Road
Marietta, GA 30007,

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Taxpayer.

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FINAL ORDER

The Revenue Department assessed State lease tax and State, Montgomery County and City of Montgomery sales tax against Cornerstone Medical, Inc. ("Taxpayer") for the period January 1, 1988 through December 31, 1988. The Taxpayer appealed to the Administrative Law Division and a hearing was conducted on March 1, 1990. Andy Simmons and Scott Simmons appeared for the Taxpayer. Assistant counsel Gwendolyn B. Garner represented the Department. This Final Order is entered based on the evidence and arguments submitted by the parties.

FINDINGS OF FACT

The Taxpayer sells and leases oxygen, oxygen concentrator machines and other medical equipment. In most cases, a physician contacts the Taxpayer and orders the necessary equipment for a particular patient. The Taxpayer then delivers the equipment to the patient and later receives a formal prescription order from the physician.

Most of the Taxpayer's customers are Medicare patients. Consequently, Medicare pays a large portion of the sales price or

rental fee charged by the Taxpayer. The balance is billed by the Taxpayer to the patient/customer.

The Taxpayer filed delinquent sales and lease tax returns and failed to pay the tax reported thereon for the period in question.

The Department subsequently entered the assessments in issue based on the delinquent returns. The Taxpayer appealed to the Administrative Law Division subsequent to an informal conference with the Department's Sales and Use Tax Division.

The Taxpayer argues that the oxygen is exempt from sales tax under the "drug" exemption set out at §40-23-4.1. The Taxpayer also argues that the oxygen concentrator machines process tangible personal property, i.e., oxygen, and thus should be taxed at the special one and one-half percent machine rate levied at §40-23-2(3).

The Taxpayer further contends that it should not be required to pay sales and lease tax because federal law indirectly prevents it from collecting sales or lease tax from its Medicare patients.

The Taxpayer asserts that Medicare has a schedule of maximum charges for each item, and will generally pay approximately eighty percent of the amount allowed. according to the Taxpayer, the seller is prohibited by federal law from collecting more than the remaining twenty percent from the customer. For example, assume that the maximum Medicare charge allowed for a leg brace is \$100.00. If the Taxpayer charged the full amount, Medicare would pay \$80.00 and the Taxpayer could charge the patient a maximum of

\$20.00, for a total maximum charge of \$100.00. The Taxpayer would be prevented from collecting any additional sales or use tax in excess of the \$100.00 charged for the brace.

CONCLUSIONS OF LAW

Section 40-23-4.1 exempts from sales tax any medicine for human consumption or intake when the medicine is prescribed by a physician and the prescription is filled by a licensed pharmacist.

However, while the oxygen in question may be ordered or prescribed by a physician, the exemption does not apply because the prescription is not filled by a licensed pharmacist, but rather by the Taxpayer. Accordingly, the oxygen is not exempt from sales tax under §40-23-4.1.

Also, §40-23-4.1 applies to sales tax only. The lease tax law contain no similar exemption. Thus, the Taxpayer would owe lease tax on the oxygen even if it was exempt from sales tax under the above section.

Section 40-23-2(3) provides that all machines used in mining, quarrying, compounding, processing and manufacturing tangible personal property shall be taxed at a reduced one and one-half percent rate. The Taxpayer argues that the oxygen concentrator machines process oxygen, and thus should be subject to the reduced rate. However, the machines do not process oxygen, but merely dispense it in varying degrees to the patient. Accordingly, the machines must be taxed at the general rate.

Also, the lease tax law does not contain a reduced machine rate. Consequently, all equipment leased by the Taxpayer must be taxed at the general four percent lease tax rate.

Sales tax is a consumer tax, but the seller is responsible and liable for payment of the tax to the Department, see §40-23-26. Thus, the Taxpayer must pay sales tax on its retail sales, and cannot be relieved of liability if it fails, refuses or otherwise does not collect the tax from its Medicare customers.

The sales and leases to the Medicare patients are not exempt, and federal law does not prohibit the Taxpayer from charging sales tax or lease tax to its Medicare customers. Also, even if the Taxpayer is correct concerning the maximum amounts that can be collected from a Medicare customer, the Taxpayer could charge less than the maximum and thus allow for the addition of the required sales or lease tax.

The above considered, the assessments in issue should be made final as entered, with applicable interest.

Entered this 29th day of March, 1990.

BILL THOMPSON
Chief Administrative Law Judge